The Circus Comes to Town: The RTC's Affordable Housing Program and its First North Carolina Auction

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On a late June afternoon, hundreds of spectators sat waiting in the yellow heat beneath a big-top tent. Young couples fanned children with folded programs and craned to see any movement on stage. Finally as organ music filled the tent, the master of ceremonies ascended the stage and barked greetings into the microphone. The crowd was captivated. But this was not the circus they had come to see. This was Resolution Trust Corporation's Affordable Housing Program!

Since the Resolution Trust Corporation (RTC) took its first steps toward implementing the Affordable Housing Disposition Program in 1989, housing advocates, congressional sponsors, and the press have lambasted the agency's efforts to reconcile the competing statutory objectives of the program. In recent months, criticism of the program has been calmed somewhat by the RTC's success at moving huge numbers of low-priced homes in highly publicized public auctions. Unlike the RTC's earlier attempts to dispose of its affordable housing inventory, the auctions have been spared most criticism, attracting instead the fanfare and hyperbole of a big-top circus coming to town.

As part of its sales blitzkrieg covering the Northeast, Southeast, and Southwest, the RTC sponsored a series of real estate auctions in North Carolina's Research Triangle Park in late June 1991. All of the properties, ranging from undeveloped land to small shopping centers, were taken from the real-estate-owned inventories of Raleigh's failed First Federal Savings and Loan. The 107 properties eligible for the Affordable Housing Disposition Program were sold during to two days of auctioning. Under the program, low-priced single-family and multi-family homes are separated from other assets and marketed for 90 days solely to low- and moderate-income households, nonprofits, and public agencies. According to its own criteria, the RTC considered the North Carolina affordable housing auction a smashing success.

The question remains whether the auction was a success when measured in terms set by statute, housing advocates, public agencies, and the buyers themselves.

How Bank Regulators Became Housing Providers

In early 1989, President Bush unveiled a comprehensive plan to resolve the crisis in the thrift industry and, in Bush's words, "to promote a safe and stable system of affordable housing finance through regulatory reform." The President's bill was sent for review to the House banking committee, chaired by Rep. Henry Gonzalez (D-Texas). A stalwart advocate of affordable housing, Gonzalez had witnessed a dramatic decline in conventional housing assistance from the federal government during the Reagan Administration. Federal budget authorizations for housing had fallen from 5.2 percent of total budget authority during the Carter Administration to just 0.73 percent in Reagan's 1989 budget (then still in effect).[1] When the President's bill emerged from the banking committee it carried an amendment creating a 90-day right of first refusal for low-income families and nonprofit and public agencies on low-cost properties held by failed Savings & Loan institutions (S&Ls). The amendment met immediate opposition from the Administration which foresaw delay and increased costs resulting from the affordable housing provisions.

In response, Democrats in the House and Senate cited three justifications for attaching housing provisions to the bailout bill. First, Democrats would support the President if the statute were structured not simply as a bailout, but also as a restatement of industry objectives. Second, the housing program would be a means of giving otherwise wasted properties back to the taxpayers asked to fund bailout. Third, directing the properties to marginal families now would prevent the government

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from having to pay housing subsidies for the same families in the long run.

With the cost of the bailout was growing an estimated $20 to $30 million every day, President Bush relented, and on August 9, 1989, signed into law an amended version of the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA).[2] The Resolution Trust Corporation and its Affordable Housing Disposition Program were born.

An Affordable Housing Program in a Hostile Agency

The mission of the RTC is to manage and resolve failed thrifts and to dispose of any residual assets that result from resolution. In retrospect, perhaps the greatest error of FIRREA's drafters was the attention given to resolution of thrifts instead of asset disposition. Although the RTC operates under the supervision of an independent oversight board, the RTC's "exclusive manager" is the Federal Deposit Insurance Corporation (FDIC). Traditionally, the focus of the FDIC was to consult with and preserve a troubled institution and, only rarely, to attempt to sell the institution as a whole. This tradition has had a profound impact on the RTC's ability to discharge its duty as a seller of individual, low-value assets.

Also complicating the RTC's mission are Congress' three seemingly contradictory mandates. FIRREA requires that the RTC dispose of residual assets in a manner that maximizes return and minimizes losses to taxpayers; minimizes the impact on local real estate and financial markets; and maximizes the preservation of the availability and affordability of residential property for low- and moderate-income individuals.[3] Throughout the process of translating Congress' intent in the Affordable Housing Disposition Program into workable regulations and procedures, RTC staff and housing proponents have continually butted heads over how to balance these mixed mandates.

The efforts of the RTC to implement FIRREA's housing provisions were further undermined by a staff that was ideologically unsuited to the task of providing affordable housing. The former bank regulators who staffed the RTC were unversed at breaking up an S&L and selling its properties. They were also uninterested in protecting low-cost homes from real estate investors and marketing them to low- and moderate-income families. More than a year after the RTC's start-up, affordable housing sponsor Barney Frank complained that RTC officials "were offended at the notion that they should be worrying about poor people. They didn't want to be a social agency, having responsibilities that would interfere with their high finance."[4] As the housing program has grown, however, the RTC has hired a multitude of workers from other government programs serving the poor.

Outline of the Program

Under FIRREA and subsequent amendments, the Affordable Housing Disposition Program requires that the RTC give a 90-day right of first refusal on "eligible properties" to "qualified purchasers." If the RTC does not receive an acceptable offer during the 90-day period, it may sell the property on the open market.

FIRREA defines qualified purchasers as households earning no more than 115 percent of the area median income, as well as nonprofit organizations or public

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agencies. Eligibility guidelines for properties are the same as those found in sections 203(b)(2) and 221(d)(ii) of the National Housing Act. One-unit dwellings may not have an appraised value of more than $67,500; two-unit dwellings, not more than $76,000; and three-unit dwellings, not more than $92,000. Multi-family housing may have a maximum appraised value of $29,000 to $58,392, depending on the number of bedrooms.

Qualifying households may purchase single-family homes subjct to a commitment to occupy the homes as their principle residence for at least one year. The RTC may recapture 75 percent of profits if a home is sold prematurely and without good cause. Qualifying agencies and nonprofits must agree to rent or resell single-family homes to families earning no more than 80 percent of the area median income. When purchasing multi-family properties, agencies and non-profits must reserve at least 20 percent of the units for very low-income tenants, defined as households earning no more than one-half the area median. An additional 20 percent of the units must be reserved for low-income tenants, or those earning 80 percent of the area median. These percentages apply in the aggregate to all complexes purchased, which allows for some segregation of low-income tenants in a few buildings. To prevent drastic segregation, Congress has recently amended program guidelines to

Table 1. Target Incomes Calculated as Percentage of Median Area Income

Family Size	Qualifying Income(115%)	Preferred Income(80%)
1	$35,150	$24,450
2	$40,000	$27,950
3	$45,200	$34,450
4	$50,250	$34,950

require at least a ten percent low-income presence in all buildings purchased. The program also limits rent paid by low- and very low-income families to roughly 30 percent of their incomes.

The 90-day marketing period operates slightly differently for single-family and multi-family properties. Marketing of single-family residences is confined to the 90-day period, during which time the RTC considers bids on a first-come-first-served basis. When choosing between substantially similar offers, the RTC gives first preference to households, second preference to non-profits, and last preference to public agencies. After the 90-day period, all restrictions on sales are lifted.

Out of all sales functions, however, it is in marketing that the RTC has best earned its new nickname, "Ready to Change."

For multi-family properties, the RTC will only accept written "notice of serious intent" from qualifying purchasers during the period. After 90 days, organizations have an additional 45 days to submit a *bona fide* offer. The RTC then chooses the best offer or, in the event of a tie, the offer that guarantees the highest percentage of low-income residency. In contrast to the single-family rules, even if eligible multi-family properties pass through the protective marketing period unsold, residency restrictions remain effective against future for-profit purchasers.

FIRREA created clearinghouses to act as information conduits between the RTC and qualifying purchasers. These may include state housing finance agencies, district Federal Home Loan Banks, or national nonprofits approved by the RTC. Originally, the RTC Oversight Board did not contemplate that clearinghouses would participate in marketing beyond disseminating of information. By contrast, the Oversight Board has created technical assistance advisors to help more actively in matching purchasers, properties, and financing. The RTC may also enter into agreements with private real estate brokers, auctioneers, and bulk-sales specialists.

RTC Under Fire

From the outset the RTC and its housing program were beset by problems that FIRREA's drafters did not anticipate. Many S&Ls taken over had kept confusing and incomplete records, which made the process of securing title to foreclosed property long and cumbersome. To its later regret, the RTC chose to assign properties to its regional and consolidated offices based on the location of the thrift that had secured the property rather than the location of the property itself. Given the geographic dispersion of investments by failed thrifts, all fourteen consolidated offices may well be responsible for properties in Dallas, for example. At the same time, the RTC gave branch offices very little authority to approve sales. Regional offices independently could only dispose of assets with book values of less than $25,000; consolidated office staff could only sell properties worth less than $10,000.[5]

The most persistent pitfalls within the affordable housing program, however, have been caused not by statutory or organizational limitations, but by the intransigence of the RTC Oversight Board. Until early 1991, the board refused to liberalize policies on price discounting, seller financing, or marketing as permitted by statute. In each area the board justified its position by arguing that Congress' first two mandates of maximizing the return to taxpayers and minimizing the impact of RTC sales on local markets, outweighed Congress' third mandate, to maximize the availability of affordable housing. Harangued by congressional sponsors and housing advocates, the RTC grudgingly has made concessions. Ironically, the open market has been the force behind the most progressive policy changes in the program.

Changes in Pricing, Seller-Financing, and Marketing

The conundrum of the affordable housing program's conflicting mandates is nowhere more obvious than in pricing policy, yet pricing is the puzzle that the RTC, as the offspring of the FDIC, is least equipped to solve. FIRREA allows for discounting to the extent necessary to make housing sales to lower-income families and nonprofit or public agencies feasible. Still, the RTC did not allow price discounting when affordable housing sales began in early 1990. In May 1990, the oversight board allowed properties to be discounted by 15 percent after four months of marketing--one month after qualifying purchasers lost their 90-day right of first refusal. Predictably, sales prices throughout the program's first several months averaged just under 100 percent of appraised value, or $42,000.[6] Not until discounts were increased to 20 percent after "some reasonable marketing" did sales prices drop to 93 percent of appraised value, or $35,700, during the last quarter of 1990.[7]

The pressure to liberalize discounting policies increased through early 1991 and culminated in an amendment to FIRREA that allowed the RTC to set prices on single-family properties without regard to any minimum purchase price.[8] Although housing advocates lobbied the RTC on ideological grounds, the economics of carrying costs provided a far stronger argument for discounting. Using the carrying costs on HUD-foreclosed homes as a proxy, the RTC incurs about $18.25 a day on each eligible property.[9] With 7,500 single-family homes in the program in May 1991, the RTC was paying about $137,000 per day to carry its inventory. Probably more in response to these costs than to the calls of housing advocates, the RTC began to sell homes at deep discounts. By the end of August 1991, the average price of a single-family home had dropped below $25,000, or just 67.4 percent of appraised value.[10]

Seller-financing has developed at much the same pace as pricing policy, slowly at first, but more rapidly of late. Because Congress had notice from Housing and Urban Development, Farmer's Home Administration, and Veteran's Administration housing programs that seller-financing would be a necessary evil of selling to qualifying families and nonprofits, FIRREA allowed below-market-rate mortgages to be taken by the RTC on affordable properties. However, in its "Strategic Plan for the RTC," the oversight board viewed seller-financing as a marketing tool to be used only when banks would not lend and only if the cost of financing is offset by a higher purchase price. In early 1990, the board imposed a requirement that all seller-financed loans be salable on the secondary market within one year, effectively precluding the use of flexible underwriting standards with low-income buyers. Finally, more than a year into the program, the oversight board approved up to $250 million in seller-financing for eligible properties with 5 percent down payments and below-market interest rates for families who were already renting the homes they would buy.

Even since the agency's change of heart, financing arranged by the RTC has been slow to materialize because of organizational delays. Sales of securitized packages of nonconforming mortgages required an amendment to FIRREA, granting RTC employees immunity from securities violations. Reservations of mortgage revenue bonds issued by state housing agencies resulted in commitments of almost $200 million by August 1991, though gun-shy banks in the Southwest had been willing to lend only a fraction of that amount. Wary of becoming a long-term lender because its statutory life extends only to 1996, the RTC currently will finance sales only when no private lender comes forward. The RTC almost always avoids that situation by enticing first-mortgage lenders with "soft second" mortgages of 5 to 20 percent of the sales price.

Out of all sales functions, however, it is in marketing that the RTC has best earned its new nickname, "Ready to Change." At the close of 1990, the RTC took stock of its efforts and found that 75 percent of its properties in number represented only 10 percent of the dollar value of its inventory and that only one percent of the RTC's proceeds were derived from affordable housing sales.[11] The RTC was acquiring low-value properties at approximately three times the rate it was selling them.[12] In response, the agency set a goal of selling 80 percent of its properties worth less than $100,000 by June 30, 1991.[13]

In order to meet its goal, the RTC planned more than 100 sales events to dispose of 9,000 affordable properties throughout the Northeast, Southeast, and Southwest during 1991. At affordable housing fairs, the agency prequalified families on the spot and provided information about area properties and financing. At silent auctions, qualifying families submitted sealed bids on advertised homes. At absolute auctions, such as the one staged in North Carolina, competitive bidding began at $5 and continued until every property on the block was sold. To support these events, the RTC signed contracts with nearly 100 government agencies and nonprofits to act as clearinghouses and technical assistance advisors. The RTC set up booths offering bilingual services in Houston supermarkets and at the Texas state fair. The agency began publishing its own newsletter, *The Silver Lining*, for bankers, nonprofits, local governments, and brokers. Even high school cheerleaders and bands were recruited to perform at auctions.

The RTC met its goal. By June 30, 1991, contracts had been signed on 85 percent of the 5,200 single-family homes that were on the books at the end of 1990. As those who prepared for or participated in the North Carolina auction can attest, the pace of sales was staggering. When the RTC approached the North Carolina Housing Finance Agency (NCHFA) in late May about hosting the auction, the RTC had experienced an 80 percent increase in sales during the preceding month.

Preparation for the North Carolina Affordable Housing Auction

The affordable housing auction held in Research Triangle Park on June 22 and 23, 1991 was among the first auctions sponsored by the RTC Mid-Atlantic Consolidated Office in Atlanta. NCHFA, which had previously contracted to act as an RTC clearinghouse, was given notice of the auction just four weeks before the first bids were cast. The RTC offered some support out of Atlanta, but responsibility for publicity, bidder prequalification, and inventory preparation fell mainly on Hudson & Marshall, the Georgia auction company under contract with the RTC; First Federal Savings & Loan, the Raleigh S&L which owned all the real estate to be auctioned off; and NCHFA. NCHFA in turn contracted out much of the prequalification of buyers to the Downtown Housing Improvement Corporation of Raleigh, the Durham Affordable Housing Coalition, and the Orange Community Housing Corporation.

Even before the auction team knew the size of the inventory or the financing available, newspaper and

Table 2. The North Carolina Auction in a Nutshell

Dates	June 22-23, 1991
Number of Properties Sold	99
Average Appraised Value	$67,720
Average Sales Price	$54,300
Average Buyer Income	$30,170
Bids per Property (Approximate)	8
Total Proceeds (Preliminary)	$5,400,0000

radio ads were run and stories appeared in the local press. NCHFA set up a toll-free phone line to receive inquiries, and Hudson & Marshall scrambled to print-up a brochure for distribution. The RTC gauged that 300 prequalified bidders would be needed to support sales comparable to previous auctions. Instead, NCHFA was swamped with more than 2,000 inquiries, resulting in 1,000 families interviewed and 800 prequalified to bid. Hudson & Marshall sponsored a "buyer's awareness preview" outside Raleigh a week before the event to familiarize bidders with the properties and the auction process; the crowds were five times that expected, backing up traffic all the way to Interstate 40.

Prequalification interviews for bidders lasted thirty minutes and consisted of three steps. Staff determined if the income figures supplied by the family fell below the program limit of 115 percent of the area median, which in the North Carolina auction ranged from $35,150 for a single-person household to $50,250 for a family of four. Very few families exceeded the limits. Second, staff calculated the maximum bid a family could offer based on their income, current debts, and financing available. Finally, staff attempted to answer questions about the auction process and the homes available. Unfortunately, prequalifiers had little information to offer. Virtually nothing was known about the properties other than their location and size and that many were new townhouses built by bankrupt developers. Though no inspections were performed, prequalifiers learned that some homes still lacked carpeting or bathtubs. RTC policy prevented bidders from learning the appraised values of the properties.

Two financing packages were available to bidders. The RTC was willing to provide 30-year, fixed-rate mortgages at 9.75 percent to purchasers who could not find private financing. Families earning below 80 percent of the area median income would pay 3 percent down; other qualifying purchasers would pay 5 percent down. The RTC would pay all closing costs and mortgage insurance, leaving buyers to pay property taxes, title insurance, and homeowner's dues. NCHFA had reserved $500,000 for first-time home buyers who earned less than 80 percent of the median income. The NCHFA's 15-year, fixed-rate financing of 80 percent of the sales price could be combined with a second mortgage from the RTC for 15 percent of the price on the same terms. Winning bidders were not required to use either RTC or NCHFA financing, and it appears few did.

Results of the Auction

The bidders assembled under the big-top tent at the affordable housing auction could not be described as a crowd of welfare recipients or "the working poor," nor were they a herd of disguised yuppies. It appeared that the RTC had achieved the same economic and racial mix that characterized earlier fields of bidders in Boston, Savannah, and Austin. However, winning bidders at the North Carolina auction appear to have been decidedly more middle-class than RTC buyers nationwide. Preliminary results of the auction show the average income of a North Carolina buyer was $30,500, or 87 percent of the area median.[14] For the first twelve auctions in the mid-Atlantic region, buyer income averaged $23,900, or 69 percent of the area median.[15] Nationwide in June, the average buyer incomes was just $23,200, or 61 percent of the national median.[16]

The jump in incomes of North Carolina buyers is partly attributable to the quality of the housing sold. Whereas homes sold in Savannah required major structural repairs and New Orleans properties were being used as crack houses, most North Carolina properties were recently constructed in healthy neighborhoods. Still, price as a percentage of appraised value, which should remain constant, was slightly higher in North Carolina than in other regions. Although in June the RTC was collecting under 78 percent of appraised value nationwide,[17] properties in June's auction sold for 80.2 percent of appraised value.[18] The $5.4 million in bids that the RTC accepted at the auction set a record for affordable housing sales, representing a whopping 105 percent of the book value of the 107 properties.

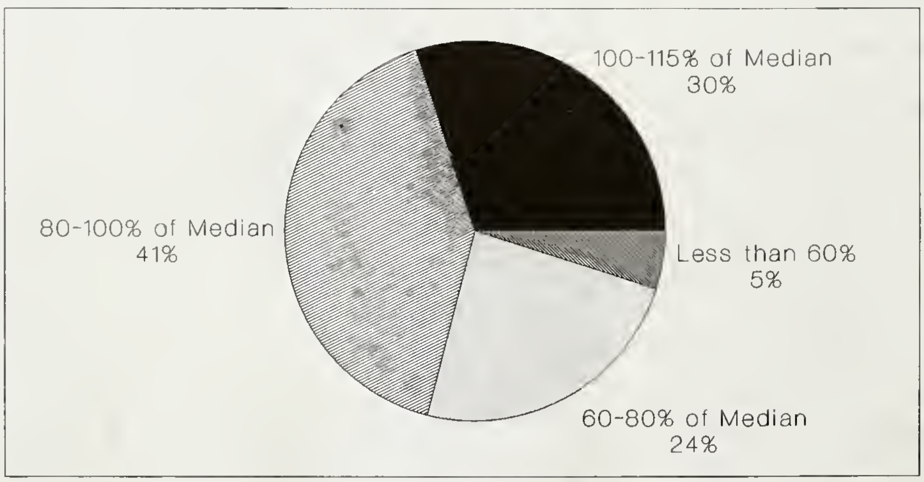

Figure 1. Income of Buyers as a Percentage of Median Income

Conclusion: Is the RTC Fulfilling Its Mandate?

After the North Carolina auction drew to a close and the big-top tent was rolled up for transport to the next town, one had to wonder if this was what Congress had in mind when it created the Affordable Housing Disposition

Program. Strange as its means were, had the RTC finally managed to reconcile its competing statutory mandates?

There is no doubt that the auction strategy serves the program's first goal of maximizing the return to taxpayers on the sale of properties. To illustrate, the RTC settled for 87 percent of appraised value on single-family homes at the June auction. Prior to using auctions, the RTC was recovering about 96 percent of appraised value. However, had the North Carolina properties been marketed individually, the carrying costs incurred in just six months would have reduced the RTC's net proceeds to the 86 percent recovered in June. Through the auction, the RTC was rid of most properties in a matter of weeks. Speedy disposition of properties is even more necessary now that Congress has made single-family properties in conservatorship, as well as receivership, permanently eligible for the affordable housing program. The change will roughly double the number of units in the program's inventory.

The goal of minimizing the impact of RTC sales on local real estate markets is also probably served by the auctions. Prior to FIRREA's passage, brokers and developers feared that if the RTC dumped its real estate there would be a sharp drop in local prices. The real evil has turned out to be the uncertainty that takes hold of local markets when the RTC delays disposition of its huge inventories. The sentiment among builders and economists now seems to be, "Go ahead and get it over with."[19]

Whether auctions serve the last goal of maximizing affordable housing opportunities is, of course, the issue no one agrees on. By the words of the statute, the RTC easily meets its mandate: FIRREA requires sales to families below 115 percent of the national median, and in August the RTC was selling its single-family homes to households earning an average of 59 percent of the national median[20] The Low Income Housing Information Service has cast serious doubt on the accuracy of the RTC's reports,[21] but even so, the RTC has a 50 percent margin of safety on its income levels. Most objections to the program, therefore, are aimed at the way the RTC sells its affordable housing. The auction is a classic example of a forum where truly low-income families are easily muscled out by the middle-class or by households whose incomes understate their actual upward mobility. The disparity in buying power is more pronounced in situations where almost no information is provided on the homes to be sold.

As the RTC has struggled to implement the affordable housing program, it has been subjected to a double standard -- one based on the lenient income limits of FIRREA and the other based on the potential that housing advocates see for providing affordable homes. After a year of auctions, the RTC has lost most of its illusions of being able to sell 1,000 properties a month, all at near-market prices. By the same token, the program's detractors have become more realistic about the RTC's capacity for doing good. Soon after the North Carolina auction, program sponsor Rep. Barney Frank conceded, "We have got to compare [the program] with perfection on the one hand and nonexistence on the other."[22]

Notes

1 Special Memorandum. Washington, D.C.: Low Income Housing Information Service, February 1991, p. 10.

2 Financial Institutions Reform, Recovery and Enforcement Act of 1989, Public Law 101-73, codified at 12 U.S.C. § 1441a.

3 Id., at § 1441a(b)(3).

4 *Newsday*. December 1, 1990, p 5.

5 Donohue, Gerry. "The Inside Story," *Builder Magazine*. March 1991, p. 133.

6 "Affordable Housing Summaries." Washington, D.C.: Resolution Trust Corporation. June-August 1990.

7 Affordable Housing Summaries. October - December, 1990.

8 The Resolution Trust Corporation Funding Act of 1991, Public Law 102-18, 1005 Stat. 58. The Funding Act actually amended the Federal Home Loan Bank Act, just as FIRREA did. However, for simplicity FIRREA is treated as the amended legislation.

9 "Few of the Working Poor Get Homes in S&L Rescue Plan." New York Times. June 26, 1991, Sec. A-1.

10 Affordable Housing Summary. August 1991.

11 Report by the Task Force on the RTC to the Subcommittee on Financial Institutions Regulation, Supervision and Insurance and to the Committee on Banking, Finance and Urban Affairs. March 11, 1991, p. 28.

12 Task Force Report, p. 22.

13 BNA's Banking Report. (April 1, 1991) Vol. 56, No. 13, p. 602.

14 Data provided in November 1991 by the RTC's Mid-Atlantic Consolidated Office. Because many successful bidders were not ultimately able to purchase after income or credit discrepancies were discovered, it can be assumed that many sales reported by the RTC either did not close or are still in the process of being closed.

15 Wiles, O. Jesse. "RTC's affordable housing auctions provide a solution to meet many needs." *Community Enterprise*. Atlanta: Federal Home Loan Bank (September 1991) Vol. 2, No. 3, p. 11.

16 Affordable Housing Summary. June 1991.

17 Affordable Housing Summary. June 1991.

18 RTC data, note 14.

19 "Current Developments", *Housing& Development Reporter* (August 19, 1991), p. 257. (reporting on testimony of Paul Barru, Chairman of the National Associationn of Home Builders' Mortgage Finance Committee before the Task Force on the RTC); and Vandell and Riddiough. "The Impact of RTC Dispositions on Local Housing Real Estate Markets", *Housing Policy Debate* (1991) Vol. 1, No. 2, p. 49.

20 *Silver Lining*. Washington, D.C.: Resolution Trust Corporation. (September/October 1991) Vol. 1, No. 1, p. 6.

21 *The New York Times*. June 26, 1991, Sec. A-1.

22 *Silver Lining*, p. 4.